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**ARIZONA CORPORATION COMMISSION**

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December 6, 2005

Chairman Jeff Hatch-Miller  
Commissioner Marc Spitzer  
Commissioner William Mundell  
Commissioner Mike Gleason

**Re: Under-funded pension plans at Arizona utilities; Docket No. E-01345A-05-0816**

Dear Colleagues:

As part of its recent filing requesting a 20 percent rate increase, Arizona Public Service reported that its pension plan has become significantly under-funded<sup>1</sup>. As a result of this news, I asked Staff to examine whether two of Arizona's other large utilities also have pension funds that are under-funded.

I believe the answer requires further action and discussion by the Commission.

According to information reported by the Companies<sup>2</sup>, both Southwest Gas and Tucson Electric Power have seen their pension funds fall behind, and these utilities, like APS, are also experiencing some degree of under-funding of their other post employment benefits such as health care benefits and life insurance.

Specifically, the latest publicly available figures show that TEP's Pension Benefit Obligation is under-funded by \$47 million, and its other post employment benefits category is under-funded by \$69 million. Southwest Gas' pension plan is under-funded by \$76 million, while it reported that its other post employment benefits are under-funded by \$18 million. Attached to this letter is a spreadsheet showing the pension information for APS, TEP and Southwest Gas.

Given the possibility that these three utilities may be representative of other utilities with pension plans, and given our duty to address such problems before they worsen, I believe we should determine the extent of this problem across all Class A utilities and analyze how the utility pensions became under-funded. For instance, I would like to know whether any of these utilities experienced **over-funded** pension plans in the late 1990s, and if so whether those funds ultimately were dividend-ed out to shareholders or reported as income. Additionally, the Commission may want to ask whether any utilities ever considered creating a rainy day fund to

<sup>1</sup> According to publicly filed documents, APS' pension plan is underfunded by \$472 million.

<sup>2</sup> From Securities and Exchange Commission website, the Federal Regulatory Commission Form 1, and/or the Company's annual reports; information as of 12/31/04.

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“save” their over-funded pension funding amounts in order to prepare for times such as this when lower interest rates and increased health care benefit costs have contributed to the under-funded status of these plans.

Among other steps, we could instruct Staff to investigate the pension liability plans of all Class A utilities through a generic docket.

Thank you for your consideration of this matter.

Sincerely,

A handwritten signature in black ink, appearing to read "Kris Mayes", written in a cursive style.

Kris Mayes  
Commissioner

Cc: Ernest Johnson  
James Dorf  
Brian McNeil  
Heather Murphy

PENSION INFORMATION  
ALL AS OF 12/31/2004

	In Millions		
	ARIZONA PUBLIC SERVICE	TUCSON ELEC POWER	SOUTHWEST GAS CORP.
<b>PENSIONS</b>			
Pension Benefit Obligation	1,454	182	369
Fair Value of Plan Assets	982	135	293
OVER (UNDER) FUNDED	(472)	(47)	(76)
Actual Pensions Paid in 2004	45	6	9
<b>OTHER POST EMPLOYMENT</b>			
Other Post Employment Benefit	536	69	34
Fair Value of Plan Assets	352	0	16
OVER (UNDER) FUNDED	(184)	(69)	(18)
Other OPEB Paid in 2004	14	1	2